United States Court of Appeals

for the Second Circuit

APPELLEE'S BRIEF

74-2242

IN THE

United States Court of Appeals

For the Second Circuit

NORMAN RICH, SHELDON SCHIFF and HOWARD SCHIFF, as trustees of the West Side Corp. Profit Sharing Plan, SIMON MARGULIES, LOUIS MARGULIES, MARILYN MARGULIES, CHARLES SHURPIN, and LILLIAN SHURPIN, on behalf of themselves and all others similarly situated,

Plaintiffs-Appellants,

against

NEW YORK STOCK EXCHANGE, LADENBURG THALMANN & CO., ARTHUR LEVINE, SOL LEIT, ALLEN SOLOMON and JOEL KUBIE,

Defendants-Appellees.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR APPELLEES

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Statement of Issues for Review

1. When plaintiffs have conceded that there is agreement as to all material facts, may a District Court grant summary judgment to defendants on grounds not urged by defendants where the Court finds that the second amended complaint fails to state a claim on the conceded facts, even under a liberal construction of the second amended complaint—amended once as a matter of right and a second time pursuant to the Court's order on defendants' motion for a more definite statement?

2. Where a member brokerage organization may have a net capital deficiency, is it within the broad discretion of a national securities exchange under section 6 of the Exchange Act to approve corrective action short of suspension, including transfer of margin accounts to another member organization, in order to reduce liabilities?

3. Does Rule 10b-5 compel disclosure by the national securities exchange of such corrective action to customers of the brokerage firm?

4. Do plaintiffs who have received full recovery of their securities, or the cash equivalent, from the Securities Investor Protection Corporation ("SIPC") in respect of their brokerage accounts have any provable damages against defendants as a matter of law for the delay of SIPC in processing their claims in liquidation?

Statement of the Case

This is an appeal from the judgment of the United States District Court for the Southern District of New York, Hon. Charles L. Brieant, entered on August 2, 1974, dismissing the second amended complaint for failure to state a claim upon which relief could be granted on the conceded facts and for the reasons set forth in a memorandum opinion reported at 379 F.Supp. 1122. (A 125a)

The action was brought on October 31, 1973, purportedly as a class action by several customers of Weis Securities Inc. ("Weis") against the New York Stock Exchange, Inc. (the "Exchange"), Ladenburg Thalmann & Co. ("Ladenburg"), and Arthur Levine, Alan Solomon, Sol Leit and Joel Kubie, officers and directors of Weis. Plaintiffs Norman Rich, Sheldon Schiff and Howard Schiff (as trustees of the West Side Corp. Profit Sharing Plan), Charles Shurpin, and Lillian Shurpin were customers of

Weis in April and May, 1973, the period immediately preceding the liquidation proceedings commenced in respect to Weis on May 24, 1973 by SIPC.[1] Weis was a member organization of the Exchange. Ladenburg is also a member of the Exchange.

Before the date on which defendants were required to answer or move with respect to the complaint, plaintiffs served an amended complaint. The amended complaint, like the initial complaint, was so vague and ambiguous that the District Court granted the Exchange's motion for a more definite statement and directed plaintiffs to file a second amended complaint setting forth the specific provisions of the Securities Exchange Act of 1934, the rules and regulations thereunder and the statute or common law duty allegedly violated by the Exchange. (A 30a, ¶ 3)

The second amended complaint complains only of the defendants' conduct "in or about April and May, 1973." (A 10a, ¶ 30) The depositions of plaintiffs show that the theory of each of plaintiffs' claims was drawn from a series of articles by Robert Metz published in *The New York Times*, which articles prompted plaintiffs to sue. (Schiff 33-35; Shurpin 82-85; A 37a)[2] The Metz articles described transfers of margin accounts of Weis customers to Ladenburg, in the period preceding the SIPC liquidation to improve Weis' financial condition, and with the approval of the Exchange.

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[1] By stipulation and order dated April 16, 1974, plaintiffs Simon Margulies, Marilyn Margulies and Louis Margulies discontinued with prejudice their action against the defendants. (A 31a, ¶ 3)

[2] Copies of the deposition transcripts of the examinations of plaintiffs Charles Shurpin, Sheldon Schiff, Norman Rich and Robert Bishop and the transcript of oral argument were made a part of the Record on Appeal by stipulation dated November 13, 1974. When reference is made to such transcripts in this brief, it is to the specific deposition and page, *e.g.*, Bishop 24 or to the transcript of argument and page, *e.g.*, Tr. 5.

The second amended complaint purports to allege five causes of action based upon common facts. Each speaks of a breach of duty for the benefit of the "tippees" or privileged customers. (A 10a-14a, ¶¶ 31, 34, 37, 4[illegible]) In substance, plaintiffs allege that in April or May, 1973, the Exchange, Ladenburg and the individual defendants had knowledge that Weis was in violation of the net capital requirements of the Exchange and was in financial difficulty. Allegedly the defendants thereafter conspired and made use of such "inside information" (A 11a, ¶ 34) by notifying certain privileged customers of Weis of its "difficult financial position, and of its imminent dissolution and advised and aided those privileged customers to transfer their accounts to various other brokerage firms," including Ladenburg. (A 11a, ¶ 31) The second amended complaint concludes that such conduct violated section 6 and section 10 of the Exchange Act and Rule 10b-5 thereunder. Liability is also premised on state law claims for fraud and breach of contract.

By April 23, 1974, defendants completed pretrial examination of plaintiffs, and the Exchange had produced the Exchange's entire files on Weis pursuant to plaintiffs' document request, and Robert M. Bishop, a senior vice president of the Exchange, had appeared for examination by plaintiffs. The Exchange then moved for summary judgment on the ground that plaintiffs had no provable damages. Ladenburg joined in the motion. (A 54a) Pretrial examination of plaintiffs had revealed that their claimed damages were entirely speculative. As a direct result of the Securities Investor Protection Act of 1970 (the "Protection Act") and of the corrective measures approved by the Exchange immediately prior to the liquidation, the plaintiffs, and all Weis customers similarly situated, obtained a full recovery, in cash or securities, for the value of their accounts with Weis on the date the liquidation proceeding was commenced. Moreover, on the basis

of this Court's decision in *Levine* v. *Seilon, Inc.*, 439 F.2d 328 (2d Cir. 1971), plaintiffs were entitled to no recovery under the theory asserted in the second amended complaint. Since plaintiffs' theory of damages—that plaintiffs were entitled to be "tippees"—has no foundation in section 6 of the Exchange Act, the Exchange's memorandum in support of the motion contained no discussion of liability under section 6.

In a well-reasoned decision, the District Court entered judgment for the defendants, relying, in part, upon this Court's opinion in *Levine*. The District Court's reading of the second amended complaint was, however, more liberal than was the Exchange's. The District Court concluded that plaintiffs pleaded a cause of action for the Exchange's failure properly to discharge its duties under section 6 of the Exchange Act to suspend or discipline Weis from "the time that the Exchange received notice of Weis' difficulties" in mid-April, 1973. (A 134a) In view of the statement made on oral argument by Mr. Julien, attorney for plaintiffs, that plaintiffs "considered authentic" (Tr. 4) the description of the Exchange's action contained in the Metz article (A 37a-38a), which Mr. Julien asserted was substantiated by the documents, the District Court was justified in holding that there was no substantial disagreement among the parties regarding the material facts. Moreover, plaintiffs had taken no exception to affidavits, documents or exhibits submitted by defendants in support of the summary judgment motion. Neither side had submitted a statement or counter-statement pursuant to 9(g) of the Local Rules of the District Court, and neither side objected to the failure of the other side to submit such a statement. Since the only question was a question of law, the District Court properly entered summary judgment on the ground that the "Exchange's efforts to aid Weis did not constitute a failure to fulfill its obligations." (A 136a)

Even though the legal principle relied on differed from what defendants urged, the District Court did not operate in a vacuum. It heard argument on the section 6 question and requested submissions from the Exchange of certain related legal materials. The District Court's determination that the second amended complaint failed to state a claim made it unnecessary to decide whether plaintiffs had any provable damages. (A 129a) Although the individual defendants did not join in the summary judgment motion, the judgment was granted in their favor as well because the same reasoning which precluded liability against the Exchange and Ladenburg also precluded liability against the individual defendants. (A 139a)

In addition to affirming the judgment for the reasons set forth in the opinion of the District Court, this Court can also affirm on the ground not reached by the District Court, but urged on the motion, that plaintiffs have no provable damages. The record establishes that plaintiffs received from SIPC all of their securities or the cash equivalent. The damages for which recovery is sought are based upon speculation and conjecture. In the absence of actual damages, prejudgment interest should not be recoverable. Moreover, it would be inconsistent with the Protection Act, the administration of which caused the delay in processing plaintiffs' claims, to permit an interest recovery based upon the delay.

Statement of the Facts

Defendants' motion for summary judgment was based primarily upon documentary evidence produced by the plaintiffs and plaintiffs' own testimony given during their examinations on oral deposition. In addition, the Bishop deposition and the affidavit of James W. Giddens, Esq., counsel to the SIPC trustee in liquidation of Weis, were

submitted as background information, and the affidavit of Russell E. Brooks, Esq., was submitted to provide a summary of the case's procedural history. Marvin G. Pickholz, Esq. also submitted an affidavit on behalf of Ladenburg joining in the motion and setting forth certain relevant authorities. At no time did plaintiffs object to the sufficiency or accuracy of any such affidavits and, indeed, they conceded the correctness of the Exchange's statement of the facts.

Action by the Exchange

In mid-April, 1973, the Exchange was informed by several principals of Weis that the company's profit and loss reports to the Exchange may have been understated by several million dollars for an unknown period of time. (Bishop 24-25) The Exchange immediately undertook intensive efforts to determine the extent of Weis' financial difficulties and to improve its capital position to insure continued safety for customers.

One principal means of achieving this was a proposed merger of Weis with Ladenburg. To insure capital compliance and thereby customer safety pending the merger, Weis proposed delivery of its margin accounts to other broker-dealers to quickly reduce its aggregate indebtedness and thereby reduce the amount of capital necessary to support the firm's liabilities. (Bishop 42-43) The Exchange concurred in the proposal as a time-tested technique to reduce liabilities, which had been successful in the past in restoring stability to financially troubled firms. (A 55a) In order to achieve the most significant improvement in the shortest period of time, Weis apparently chose to deliver out the accounts with the largest debit balances to Ladenburg. (Bishop 44-45)

These efforts were unsuccessful and on May 24, 1974 Weis was suspended by the Exchange and court action

was initiated by SIPC under the provisions of the Protection Act. The Act has no provision for either the transfer out of customer accounts or the purchase or redemption of unavailable securities. (A 40a-41a, ¶¶ 8, 9)

Full recovery by plaintiffs under SIPC

Plaintiffs received from SIPC their actual securities in accordance with the formula mandated by the Protection Act. To the extent that there were shortages, after deducting the debit balance (amounts owed to Weis) in the case of the Shurpins who maintained margin accounts, plaintiffs received payment in cash at the May 24 values, without commission charges, in lieu of the available securities. Thus, before commencing this action, plaintiffs received the full value of their Weis accounts in cash or securities. (Shurpin 43-44; Schiff 74, 189; Rich 51)

Despite the undisputed fact that plaintiffs have already obtained recovery under the Protection Act, plaintiffs feel that but for the Weis liquidation, which froze their accounts for a short period while the 35,000 claims were being processed, they would have made large sums of money in the market. One plaintiff is sure that he would have foreseen the oil crisis and bought small oil stocks appreciating 100, 200 or 300 per cent. (Shurpin 35-36, 51-52) Another testified to possible transactions bringing returns of 10% on the cash and securities in the account. (Schiff 248-249) Yet, none of the plaintiffs could furnish any particulars or documents regarding the conjectured transactions. Indeed, one plaintiff finally conceded, "It's conjecture, speculative. We don't know." (Schiff 247) And another described his damages as "surmise." (Rich 68)

ARGUMENT

I

The District Court properly entered summary judgment for defendants, although on a ground not specifically urged, because even under a liberal construction of the second amended complaint, the undisputed material facts showed there was no claim upon which relief could be granted.

A. Plaintiffs conceded to the District Court that there was no dispute as to the facts material to the issues raised by the second amended complaint.

Mr. Julien commenced his argument on the summary judgment motion by stating that plaintiffs' "considered authentic" *The New York Times* article by Robert Metz, which the District Court would find was substantiated by "the documentation in this case." Mr. Julien said:

> Mr. Julien: Let me tell you briefly what our case is about. This is an action against the Stock Exchange, a brokerage firm and several of the officers of Weis & Company, a brokerage firm that was registered with the stock exchange.
>
> It arises from the following facts, and I may state to you, that annexed to the papers submitted by my opponents with respect to their motion for summary judgment, you will find a rather excellent factual background taken from a newspaper account, strangely enough, but considered authentic by both of us. The article is by Robert Metz in the New York Times which they annexed to their papers, and once you come to read the documentation in this case, you will find this is an excellent factual background, but to state it succinctly, this is what happened here. (Tr. 4-5)

After contending that plaintiffs complained about the Exchange's failure to supervise Weis commencing in 1971, a contention for which the District Court found no support in the second amended complaint, Mr. Julien continued his statement of the facts as follows:

> So . . . in April of 1973, the Stock Exchange is now told that Weis & Company's capitalization is below its capital structure requirements and thereupon certain things transpire which become the springboard of the causes of action which we maintain.
>
> The Stock Exchange and Weis & Company arrange—
>
> THE COURT: Weis told the Stock Exchange in April?
>
> MR. JULIEN: They say so. They say that is what happened.
>
> They arrange with the Stock Exchange consent that some accounts of Weis & Company chosen at random, apparently, are to be transferred to other brokerage houses, principally the co-defendants Ladenburg, Thalmann and so forth, the other stock brokerage firm. The purpose was to reduce the indebtedness of Weis & Company and apparently try to bring them up to an appropriate level.
>
> THE COURT: These were margin accounts they were transferring?
>
> MR. JULIEN: Yes, large margin accounts. (Tr. 5-6)

After Mr. Julien had completed his discussion of the class action issues the District Court inquired, "What do you claim that the Defendant Stock Exchange should have done in April 1973 faced with the knowledge that Weis was in violation of its net capital rules?" The following colloquy occurred as a result:

> MR. JULIEN: By law, if it is to be a void [sic] being a tippor, by law it must publicly disclose. We

all have to be in the same position.

THE COURT: What should they have disclosed, that they are under-capitalized?

MR. JULIEN: Yes, and that they are arranging for transfers or trying to work out a merger with another company. It must be disclosed.

THE COURT: That wouldn't create a run on the bank?

MR. JULIEN: Sir, this is no excuse under our law. If it does or it doesn't, I, Mr. Little Investor, has the same right as their million dollar investor to transfer my account. The rate [sic] should not go with that kind of handicap.

THE COURT: What is the basis for imposing the liability on Ladenburg?

MR. JULIEN: They participated in the same arrangement whereby they took some of the accounts from Weis & Company.

THE COURT: In other words, the Stock Exchange by your theory called them up and said Weis is in trouble and they have to unload and we want you to take 100 of their largest margin accounts and Ladenburg says okay, send them over. Is that what happened here?

MR. JULIEN: I think it is a little more and possibly a little less. I am not saying here that the Stock Exchange called Ladenburg and said, you take it over. I am saying that the Stock Exchange approved that kind of transaction and that Weis and Ladenburg worked it out so Ladenburg knew what they were doing. Just like in the Gulf Sulphur Case, they become a tippee too. They have the inside information. Some use is made of it, they therefore become liable. (Tr. 18-19)

This language from Mr. Julien's oral argument is included to show that plaintiffs' contention on appeal, that they disputed the material facts relied upon by the District

Court and that further discovery was required, is contrived. The news article submitted by the Exchange, which Mr. Julien advised the District Court plaintiffs "considered authentic" and an "excellent factual background" substantiated by the documentation submitted on the motion, includes substantially the same facts set forth by Mr. Julien in his argument.

Mr. Metz explained that transfers of margin accounts "were undertaken in a legitimate effort to reduce customers' margin indebtedness. This, in turn, would reduce Weis' indebtedness in that Weis, like all other brokerage firms, borrowed from banks to finance loans made to customers." (A 37a) Further the large accounts were presumably chosen by Weis "because a relatively few transfers would have a large impact" with the result that only 70 accounts remained in Weis with dollar amounts in excess of the limits of the Protection Act. (*Id.*) Plaintiffs in their depositions also conceded that the transfer of margin accounts was "to lower the debts of Weis Securities, at the bank. . . ." (Shurpin 89)

The District Court was entitled to consider the admissions of plaintiffs and their counsel in determining whether there was a genuine issue of material fact. *Missouri Pacific R. Co.* v. *Nat'l Milling Co.,* 409 F.2d 882 (3d Cir. 1969). The facts in *Missouri Pacific* are very similar to those here. Plaintiff moved for judgment on the pleadings. In its brief and argument to the court, plaintiff admitted that the material facts were undisputed. There being no facts in dispute, the lower court entered judgment for defendant and plaintiff appealed. In reviewing the decision, the Court of Appeals considered the "minutes of that hearing," which showed, as does the transcript here, that plaintiffs' counsel admitted that there was no dispute as to any material fact. *See also Am. Renaissance Lines, Inc.* v. *Saxis Steamship Co.,* 502 F.2d 674, 678-79 (2d Cir. 1974).

The record in this case shows that in opposing the motion for summary judgment plaintiffs also attempted

to introduce the new claim, to which they now devote a major portion of their brief, that the Exchange failed to supervise properly Weis commencing in April, 1971. (See A 42a-44a, 118a-19a) Plaintiffs' contention was specifically considered and rejected by the District Court in the following terms:

> Plaintiffs have not alleged that the Exchange had actual knowledge of Weis' financial difficulties prior to mid-April 1973, nor do they allege any facts upon which we could find that the Exchange in the exercise of due diligence should have known prior to that time. In fact, careful examination of the second amended complaint reveals that plaintiffs base their claims only on defendants' actions after actual discovery of Weis' difficulties. (A 134a)

Having rejected plaintiffs' effort to introduce at the last moment a new theory of liability, the District Court was not bound to consider facts that might be material to that theory. As the court stated in *Page* v. *Work*, 290 F.2d 323, 334 (9th Cir.), *cert. denied*, 368 U.S. 875 (1961):

> Two different theories of interstate commerce were presented to the district court on the cross motions for summary judgment. The district court rejected appellant's theory and adopted appellees' theory. . . . We are not concerned with the existence of a fact issue under appellant's theory of interstate commerce, which was rejected by the district court.

See also 3 Barron & Holtzoff, *Federal Practice & Procedure* § 1234, p. 131 (1958).

It is frivolous to suggest that there is an issue of fact as to whether the transfer of margin accounts from Weis was accepted by Ladenburg and approved by the Exchange "to aid certain favored accounts" (App. Br. 51), in view of the concessions made by Mr. Julien on oral argument. Mr. Julien specifically stated, "I am not saying here that

the Stock Exchange called Ladenburg and said, you take it over. I am saying that the Stock Exchange approved that kind of transaction and that Weis and Ladenburg worked it out. . . ." (Tr. 19) Mr. Julien reiterated, "They arrange with the Stock Exchange consent that some accounts of Weis & Company chosen at random, apparently, are to be transferred to other brokerage houses. . . ." (Tr. 6) Neither does the Metz article, which plaintiffs "considered authentic," even remotely suggest any motive but the protection of public customers and the improvement of Weis' financial situation. (A 37a)

Moreover, even if plaintiffs had suggested an intent to favor certain customers, it would have been insufficient to defeat summary judgment. It is well established that a motion for summary judgment cannot be avoided by allegations based upon speculation, conjecture and surmise. Thus, in *Applegate* v. *Top Associates, Inc.*, 425 F.2d 92, 96 (2d Cir. 1970), Judge Kaufman stated:

> To avoid summary judgment . . . a plaintiff must do more than whet the curiosity of the court; he must support vague accusation and surmise with concrete particulars.

See also Ashwell & Co. v. *Transamerica Ins. Co.*, 407 F.2d 762, 766 (7th Cir. 1969); *Dressler* v. *MV Sandpiper* 331 F.2d 130, 133 (2d Cir. 1964). The record in this case establishes beyond any doubt that plaintiffs conceded there was no dispute as to the material facts under the second amended complaint. Plaintiffs are therefore precluded from arguing on appeal that there were issues of material fact in dispute. *Halstead & Mitchell Co.* v. *United Steelworkers of Am.*, 421 F.2d 1191, 1193-94 (3d Cir. 1969).

B. The District Court was not confined by Rule 56 to application of the propositions of law argued by the parties to the undisputed facts.

The District Court acted entirely in accordance with the purpose and provisions of Rule 56 by entering sum-

mary judgment for defendants, although for additional reasons than those argued in the Exchange's motion. The transcript of oral argument (Tr. 18-20, 22-29, 34-38, and 50-51) shows that the District Court requested and heard argument from the attorneys regarding the merits of plaintiffs' claims. Indeed, the District Court asked Mr. Brooks to submit a copy of the opinion in *Independent Investor Protective League* v. *New York Stock Exchange*, 367 F.Supp. 1376 (S.D.N.Y. 1973), relating to the Exchange's duty to publicize financial problems of member organizations of the Exchange. (Tr. 24) Mr. Brooks also agreed to furnish to the Court a copy of the Exchange's net capital rules. (Tr. 27) Both were submitted by letter several days after argument of the motion with a copy to plaintiffs' counsel. (A 77a) Unless this Court finds that there was a genuine dispute as to a material fact under the second amended complaint, the judgment of the District Court should not be disturbed. It is plain from the record that such material facts were uncontested by plaintiffs and that further discovery was unnecessary.

In disposing of a motion for summary judgment, courts are not bound by "mere outworn procedural niceties." *Local 33, Int'l Hod Carriers, etc.* v. *Mason Tenders,* 291 F.2d 496, 505 (2d Cir. 1961). Where the facts are undisputed, and the issue depends solely upon a legal conclusion, resort to summary judgment is appropriate. *Willheim* v. *Murchison,* 231 F.Supp. 142, 144 (S.D.N.Y. 1964), *aff'd,* 342 F.2d 33 (2d Cir.), *cert. denied,* 382 U.S. 840 (1965); *Sadwith* v. *Lantry,* 219 F.Supp. 171, 173 (S.D.N.Y. 1963). Summary judgment can even be entered in favor of a non-moving party who is entitled to such relief. *Harcourt, Brace & World, Inc.* v. *Graphic Controls Corp.,* 329 F.Supp. 517, 521 (S.D.N.Y. 1971); *Ruby* v. *American Airlines, Inc.,* 227 F.Supp. 702, 703 (S.D.N.Y.), *aff'd,* 323 F.2d 248 (2d Cir. 1963), *cert. denied,* 376 U.S. 913 (1964). This Court has even held that on appeal it may reverse

and enter summary judgment for the non-moving party if only questions of law are involved. *Abrams* v. *Occidental Petroleum Corp.*, 450 F.2d 157, 165-66 (2d Cir. 1971), *aff'd*, 411 U.S. 582 (1973).

For the same reasons, the fact that a party "has mistaken his grounds for relief does not foreclose further consideration of his motion if it appears on the undisputed facts he is otherwise entitled to prevail. To require him to move anew under a different legal theory for judgment . . . would be wasteful of the time, energy and resources of the litigants and the courts." *Wisnouse* v. *Telsey*, 367 F.Supp. 855, 857-58 (S.D.N.Y. 1973). *See also Broderick Wood Products Co.* v. *United States*, 195 F.2d 433, 436 (10th Cir. 1952); *Board of Nat'l Missions* v. *Smith*, 182 F.2d 362, 364-65 (7th Cir. 1950); *Crowder* v. *United States*, 255 F.Supp. 873, 874 (N.D. Calif. 1964), *aff'd*, 362 F.2d 1011 (9th Cir. 1966).

In the *Board of National Missions* case, *supra*, the plaintiff sued to declare a remainder interest under a will in respect of a parcel of land. The defendant moved for summary judgment on the ground this his deed gave him fee title. Plaintiff opposed by arguing that the deed was invalid and that the will did not authorize disposition of the remainder interest. The District Court, without passing upon the validity of the deed, held that the will gave a power of sale over the disputed property. In affirming the judgment, the Court of Appeals said:

> The fact that the judgment was granted on a reason different from that assigned by the defendant is immaterial, where, as here, the motion was properly granted on the undisputed facts shown and on an issue presented by plaintiff's complaint. (182 F.2d at 364-65)

See *Mintz* v. *Mathers Fund, Inc.*, 463 F.2d 495, 498 (7th Cir. 1972).

Summary judgment is not precluded because the question of law is important, difficult or complicated. "It is for the court to decide whether further development of the facts and surrounding circumstances will assist it in making a correct determination of the question of law." 3 Barron & Holtzoff, *Federal Practice & Procedure* § 1234, pp. 127-28 (1958). On a motion for summary judgment, the court considers the entire setting of the case, including admissions of counsel, and all papers of record. An issue of fact is not material unless it has "dispositive significance" in respect of the allegations of the complaint. *Abrams* v. *Occidental Petroleum Corp.*, 450 F.2d 157, 166 (2d Cir. 1971), *aff'd,* 411 U.S. 582 (1973).

The case of *Jaffee & Co.* v. *SEC,* 446 F.2d 387 (2d Cir. (1971), cited by plaintiffs (Br. 22), is not relevant to the issues before this Court. *Jaffee & Co.* involved a petition for review of an order of the Securities and Exchange Commission disciplining petitioners for violation of Rule 10b-5. The Commission made a determination that the broker-dealer was derivatively responsible for the acts of its employees, although fair notice of such charges had not been given. This was contrary to the specific provision of 15 U.S.C. § 78a(b)(5), which required "appropriate notice and opportunity for hearing" in a disciplinary proceeding. The instant action is, of course, not a disciplinary proceeding. More important, the decision of the District Court here is based upon the admissions of plaintiffs' attorney that there was no substantial dispute as to the material facts. It would have been contrary to the purpose of Rule 56 if the District Court had declined to enter summary judgment.

C. Plaintiffs waived any objection to the sufficiency or admissibility of the evidence by their failure to move or object in the District Court.

The primary basis for plaintiffs' attack on the District Court's decision is not that the material facts relied upon

are erroneous or disputed, but that the affidavits, documents and depositions making up the record are inadmissible. This contention is extraordinary, since no objections were taken to such materials before the District Court. Plaintiffs' argument is not unlike that of the defendants in *Auto Drive-Away Co. of Hialeah, Inc.* v. *ICC*, 360 F.2d 446, 448-49 (5th Cir. 1966), where the Court stated:

> The defendants . . . do not dispute that the ICC affidavit, party admissions on file, and other materials together contain sufficient evidence to prove that their operation requires ICC authorization. . . . The defendants instead attack the admissibility of most of the materials on which the court based its judgment. . . . These objections come too late: the defendants failed to object to the introduction or use of the affidavit and exhibits below. An affidavit that does not measure up to the standards of Rule 56(e) is subject to a timely motion to strike. In the absence of this motion or other objection, formal defects in the affidavit ordinarily are waived.

Accord, Noblett v. *General Electric Credit Corp.*, 400 F.2d 442, 445 (10th Cir.), *cert. denied*, 393 U.S. 935 (1968); 6 Moore, *Federal Practice* ¶ 56.22[1] at 2817 (1974 ed.).

First, plaintiffs, without showing any prejudice to themselves, object to the fact that the Bishop deposition transcript was unsigned. Such objection is baffling since plaintiffs take no exception to the substance of his testimony. The principle reason the Bishop deposition was returned to plaintiffs unsigned was that defendants had no opportunity to cross-examine. (App. Br., Ex. A) Plaintiffs had ample opportunity after the February 6, 1974 adjournment, to complete their examination of Bishop and, for whatever reason, elected not to do so. Further, plaintiffs were aware that the deposition was unsigned when submitted on the motion, but made no objection. It is well established that

unless timely objection is made or a motion to suppress is filed pursuant to Rule 32(d)(4), "[e]rrors and irregularities in the manner in which the testimony is transcribed or the deposition is prepared, signed, certified, sealed, indorsed, transmitted, filed or otherwise dealt with by the officer under Rules 30 and 31 are waived. . . ." See *Trade Development Bank* v. *Continental Ins. Co.*, 469 F.2d 35, 44-45 (2d Cir. 1972); *Lumbermens Mutual Casualty Co.* v. *Rhodes*, 403 F.2d 2, 8 (10th Cir. 1968), *cert. denied*, 394 U.S. 965 (1969); *Valdez* v. *United States*, 326 F.2d 598 (9th Cir. 1963); *Jno. T. McCoy, Inc.* v. *Schuster*, 44 F.Supp. 499 (S.D.N.Y. 1942). *Compare McSpadden* v. *Mullins*, 456 F.2d 428, 430 (8th Cir. 1972), cited at page 31 of appellants' brief, where a motion to strike was timely made in the district court before the return date of the summary judgment motion. Here, had there been objection a signature could have been obtained. *See Chamber* v. *United States*, 357 F.2d 224, 229 (8th Cir. 1966).

Plaintiffs' citation (Br. 38) of *Blum* v. *Campbell*, 355 F.Supp. 1220 (D.Md. 1972), for the proposition that the Bishop deposition transcript is inadmissible is as curious as is the description in *Blum* of the "deposition" which was excluded from the evidence on the summary judgment motion. The Court described the excluded deposition as follows:

> In other words, on the face of the document submitted, it appears that the "deposition" of plaintiff's friend, Frederick Harvey, was taken on June 5, 1967 with Eugene Blum, the plaintiff, acting as the notary and swearing the witness and with the plaintiff's attorney being the only other person present besides the stenographer who transcribed the proceedings . . . defendant Campbell was not represented at the "deposition," . . . the same subject matter as in this case was not then involved and . . . the same parties were not then involved. See Moore on Federal Practice, 2d Ed., Vol. 6, p. 2146. This

> Court concludes that the document in question cannot be accepted either as a deposition or as an affidavit properly receivable under Rule 56 in opposition to defendant Campbell's motion for summary judgment. (355 F.Supp. at 1227)

The distinction between the facts in *Blum* and those here requires no elaboration. *Blum* is inapposite at best.

Plaintiffs' second contention is that the District Court improperly relied upon the memoranda of law, argument of counsel and unsworn letters from the Securities and Exchange Commission ("SEC") and from an official of the Exchange. It is obvious that plaintiffs' objection to these materials is misplaced. As is evident from the portion of the District Court's opinion quoted by plaintiffs (Br. 26), the District Court relied upon three factors in determining that no claim existed: (1) the uncontested facts, (2) evidence presented in affidavits, and (3) the depositions. (A 129a) The few references the District Court made to the memoranda of law (A 128a) were simply to point out facts already conceded by plaintiffs' counsel on oral argument. For example, the District Court refers to the fact that Weis "selected and transferred to Ladenburg those accounts with the largest debit balances." (*Id.*) This same fact was expressly admitted by Mr. Julien in his argument. (Tr. 6, 9) The Metz article, declared by Mr. Julien to be an accurate statement of the facts, similarly states that the transfers of margin accounts "were undertaken in a legitimate effort to reduce customers' margin indebtedness." (A 37a) This was the other issue with respect to which the District Court referenced defendants' memoranda. (A 128a)

The quotation of the District Court from a letter by the Director of the Division of Market Regulation of the SEC was clearly to explain the question of law under section 6 raised by the District Court's generous reading of the second amended complaint. The Commission's letter

merely confirms what is obvious from a reading of NYSE Rule 325, and what Metz explains in his news article (A 37a), that reduction of the amount of bank borrowings collateralized by customers' margin securities reduces aggregate indebtedness, which in turn effects a lower net capital ratio. There is no question that the Exchange approved Weis' transfers of margin accounts for this purpose; the only issue on this appeal is whether such action by the Exchange was within the scope of the Exchange's broad discretion under section 6. Plaintiffs studiously avoid this issue, as well they should. See Point II, *infra.*

Plaintiffs next argue (Br. 31) that affidavits "submitted by attorneys for a party should not be considered except insofar as they are based upon personal knowledge." Of course, the Brooks and Giddens affidavits did not purport to set forth facts concerning the Exchange's actions relating to Weis in April and May, 1973. The purpose of the Giddens affidavit was to explain the operation and limitations of the Protection Act as it applied in the Weis liquidation proceedings in this court. It is these proceedings about which plaintiffs complained, see, *e.g.*, Shurpin 286. The Giddens affidavit demonstrated the promptness with which most Weis customers, including plaintiffs, were paid in full on their accounts, and showed that 99.5% of such customers had been "satisfied in full" at the time his affidavit was sworn to. The matters in the Giddens affidavit are matters within Mr. Giddens' personal knowledge as the attorney for SIPC who functioned on them. Defendants do not contend that the Giddens affidavit is necessary to the District Court's decision; it is relevant to plaintiffs' purported damage claims, and, of course, the facts set forth are not disputed by plaintiffs.

The Brooks affidavit simply summarizes the procedural history of this action, which clearly was within Mr. Brooks' personal knowledge as an attorney in charge of the case.

That affidavit showed the following significant facts, which are otherwise of record: (1) plaintiffs amended their complaint once as a matter of right and a second time pursuant to a motion for a more definite statement; (2) three of the original plaintiffs discontinued their actions against the defendants with prejudice; (3) the Exchange produced all of its files relating to Weis in response to plaintiffs' document request and copies of all documents requested by plaintiffs were promptly furnished; (4) the deposition of Bishop was terminated at plaintiffs' request after a one-half day's examination; and (5) between February 6, 1974, when such examination and document production took place, and April 23, 1974, when the Exchange moved for summary judgment, plaintiffs conducted no further discovery.

In view of this procedural history, it should hardly be surprising that the District Court deemed it improper to permit plaintiffs to amend their complaint a third time to plead an entirely new cause of action.

D. The District Court acted within its discretion in entering summary judgment for defendants, despite plaintiffs' effort to interject a new theory of liability which would have required a third amendment to the complaint.

Plaintiffs have no more right to defeat a motion for summary judgment by raising a new theory requiring amendment of the complaint, than plaintiffs would have to amend in the absence of a motion for summary judgment. The same argument as plaintiffs make here was rejected by the Court in *Freeman* v. *Continental Gin Co.*, 381 F.2d 459, 469 (5th Cir. 1967), which stated the following:

> A busy district court need not allow itself to be imposed upon by the presentation of theories seria-

> tim. Liberality of amendment is important to assure a party a fair opportunity to present his claims and defenses, but "equal attention should be given to the proposition that there must be an end finally to a particular litigation."

See also Lilly v. *United States Lines Co.*, 42 F.Supp. 214, 215 (S.D.N.Y. 1941).

Plaintiffs' action was commenced in October, 1973. Plaintiffs amended once as of right. In December, the District Court entered an order on the Exchange's motion for a more definite statement directing plaintiffs to file a second amended complaint to which defendants could frame a responsive pleading. The pleading which was the result of that decision was before the District Court on the summary judgment motion. The criminal indictment of certain officials of Weis referred to by plaintiffs (Br. 48) was filed July 16, 1973, before the commencement of plaintiffs' action. *United States* v. *Arthur J. Levine*, 73 Crim. 693 (S.D.N.Y.). At the beginning of February, 1974, the Exchange produced for plaintiffs' inspection its entire files relating to Weis. The testimony of Robert Lynn, to which plaintiffs refer (Br. 48) is not part of the Record on Appeal. Nevertheless it was available to plaintiffs in February as a result of the document production. The Exchange's cross-claims against the individual defendants (not its answer to the second amended complaint as plaintiffs suggest at Br. 44), which alleged fraud commencing in 1971 was, of course, served on plaintiffs on December 24, 1973. In short, plaintiffs had knowledge of all the information which would purportedly support a third amendment to the complaint substantially prior to the date on which the Exchange moved for summary judgment and yet no motion for leave to amend their second amended complaint was made. No adequate justification for their delay being shown, leave to amend, had it been sought by a proper motion, would have

been justifiably denied. See Rule 15(a), Fed. R. Civ. Pro.; *Troxel Mfg. Co.* v. *Schwinn Bicycle Co.*, 489 F.2d 968, 970 (6th Cir. 1973), *cert. denied*, 94 S.Ct. 1942 (1974); *Vine* v. *Beneficial Finance Co.*, 374 F.2d 627 (2d Cir.), *cert. denied*, 389 U.S. 970 (1967).

In the *Vine* case, this Court reviewed a decision of the District Court denying leave to amend on the ground that the new information alleged in the amended complaint was within plaintiff's knowledge before argument of the motion to dismiss the first amended complaint. The Court said:

> Thus, one basis for denial of leave to amend was the bad faith of appellant in waiting to see how he would fare on the prior motion to dismiss. Although "leave shall be freely given when justice so requires," Fed. R. Civ. P. 15(a), in these circumstances, it was certainly within the district court's discretion to deny leave to amend because of "undue delay, bad faith or dilatory moves." (474 F.2d at 637)

See also Johnson v. *Sales Consultants, Inc.*, 61 F.R.D. 369 (N.D. Ill. 1973); and *Eisenmann* v. *Gould-National Batteries, Inc.*, 169 F.Supp. 862, 864 (E.D. Pa. 1958).

Plaintiffs profess surprise (Br. 44) that the District Court did not recognize that the claims asserted in *Rich* v. *Touche Ross & Co.*, 74 Civ. 772 (C.L.B.), relating to Weis' actions, and those of its officers, directors and accountants, between January, 1971 and May, 1973 (A 139a), were not also contained in their second amended complaint in the instant action. That such claims were asserted in a separate action commenced on February 19, 1974, and not by joinder of those claims or Touche Ross & Co. in the instant action, can lead to only one conclusion: plaintiffs assert "different factual claims" in *Rich* v. *Touche Ross & Co.*, as the District Court found. (A 139a)

There is an additional reason why it was proper for the District Court not to grant plaintiffs leave to amend. Plaintiffs' new theory of liability would be based upon an alleged violation by the Exchange of its statutory duties under section 6. The District Court correctly held that because of the Exchange's broad discretion to carry out its regulatory responsibilities, a complaint alleging a violation of section 6 will not be upheld unless it contains "sufficient allegations of fraud." (A 133a) *Accord, Hochfelder* v. *Midwest Stock Exchange,* 350 F.Supp. 1122, 1125 (N.D. Ill. 1972), *aff'd,* 503 F.2d 364 (7th Cir. 1974), *cert. denied,* 43 U.S.L.W. 3203 (U.S. Oct. 15, 1974); *Schonholtz* v. *American Stock Exchange Inc.,* 376 F.Supp. 1089 (S.D.N.Y.), *aff'd,* 505 F.2d 699 (2d Cir. 1974). Plaintiffs suggested to the District Court nothing that would satisfy the requirement for particularized pleading of fraud under Rule 9(b) in respect of fraud by the Exchange. Plaintiffs' conclusory allegations would be insufficient to sustain a third amended complaint from dismissal, *Segal* v. *Gordon,* 467 F.2d 602 (2d Cir. 1972); it can hardly warrant an amendment to plead such an insufficient claim. *Feldman* v. *Lifton,* CCH Fed. Sec. L. Rep. ¶ 94,870 (S.D.N.Y. 1974).

Neither *Rossiter* v. *Vogel,* 134 F.2d 908 (2d Cir. 1943), nor *Sherman* v. *Hallbauer,* 455 F.2d 1236 (5th Cir. 1972), which are cited by plaintiffs (Br. 45), suggest that conclusory allegations of fraud, in contrast to *facts* appearing in affidavits, are sufficient to defeat a motion for summary judgment or to require a district court to deny summary judgment and grant leave to amend. This Court found in *Rossiter* that the presence of fraud and the failure of consideration were shown by facts set forth in the affidavits submitted in opposition to the motion for summary judgment. Similarly, in *Sherman,* the court found ample factual basis in the affidavits to support the plaintiffs' theory. No such factual showing was ever made by plaintiffs in this action despite ample opportunity for discovery. In short,

nothing submitted by plaintiffs in their brief on this appeal suggests that they seek in their most recent charges against the Exchange to do other than to find a claim, even though each of the plaintiffs admittedly recovered the full value of his account with Weis.

II

The Exchange properly acted within its broad discretion under Section 6 of the Exchange Act in its efforts to aid Weis in April and May 1973, including its approval of the transfer of margin accounts to improve Weis' financial position; Rule 10b-5 does not preclude Exchange approval of such transfers without public disclosure.

A. Approval of transfers of margin accounts was consistent with the goal of customer safety.

It is hardly surprising that plaintiffs devote only the last four pages of their sixty-three page brief to the alleged liability of the Exchange under section 6 of the Exchange Act and Rule 10b-5. Plaintiffs seek to predicate such liability on Exchange approval of transfers of margin accounts from Weis to Ladenburg to improve Weis' "capital position, so that the firm would survive and customer safety would be assured." (A 128a) The action of the Exchange from mid-April 1973, when the Exchange was informed by several principals of Weis that Weis may have been understating its profit and loss reports to the Exchange, until May 24, 1973, when Weis was suspended from the Exchange and placed in liquidation, was immediate, was unquestionably taken in the best interests of Weis and customer safety, and was consistent with the Exchange's obligations under section 6 of the Exchange Act. Moreover, the Exchange's action could not possibly have been the proximate cause of any damage to plaintiffs, who were fully within the dollar limits of the Protection Act.

Indeed, this suit is unique in that it appears to be the first relating to discharge of the Exchange's section 6 supervisory responsibilities in the context of a SIPC liquidation.

The obligation of the Exchange to supervise its members arises from section 6 of the Exchange Act (15 U.S.C. § 78f), which provides that an exchange that seeks registration shall file an agreement "to comply, and to enforce so far as is within its powers compliance by its members, with the provisions of this chapter [the Exchange Act], and any amendment thereto and rule or regulation made or to be made thereunder." Section 6(b) requires the Exchange to adopt rules "for the expulsion, suspension or disciplining of a member for conduct or proceeding inconsistent with just and equitable principles of trade" and section 6(d) requires the SEC to grant registration to the Exchange if it appears to the SEC that "the rules of the exchange are just and adequate to insure fair dealing and to protect investors." Neither section 6 nor case law holds that courts may second-guess the Exchange's good faith enforcement of its rules.

When Congress enacted section 6, it intended that broad discretion be accorded exchanges to interpret and apply their own rules. As this Court noted recently in *Gordon* v. *New York Stock Exchange,* 498 F.2d 1303, 1306 (2d Cir.), *cert. granted,* 43 U.S.L.W. 3295 (U.S. Nov. 18, 1974) (Dkt. No 74-304):

> That Congress intended Commission-supervised exchange self-regulation to be of central importance in the scheme of the 1934 Act is emphasized by the legislative history of the Act. Both House and Senate reports stress the broad responsibility left with the exchanges to administer their own affairs. H.R. Rep. No. 1383, 73d Cong., 2d Sess. 15 (1934); S.Rep.No. 792, 73d Cong., 2d Sess. 13 (1934).

See also Intercontinental Industries, Inc. v. *American Stock Exchange,* 452 F.2d 935 (5th Cir. 1971), *cert. denied,* 409 U.S. 842 (1972). In *Intercontinental,* petitioners objected to the delisting of their stock on the American Stock Exchange, claiming that the exchange's delisting rules had not been violated. The Court of Appeals stated:

> In keeping with the Congressional purpose of making the Exchange a self-regulatory body, broad latitude must be given to the Exchange in making the critical judgment of when a company has failed to fulfill its responsibilities to such an extent that dealing on the Exchange in the security is unwarranted. . . . Since these are the rules of the Exchange, it should be allowed broad discretion in the determination of their meaning and application. (452 F.2d at 940)

The question of an exchange's discretion in enforcement of its rules has also been considered by the New York State courts in *Aronson* v. *McCormick,* 13 Misc. 2d 1077, 178 N.Y.S. 2d 957 (Sup.Ct. N.Y.Co.), *aff'd,* 6 A.D. 2d 999, 177 N.Y.S 2d 1004 (1st Dep't 1958) There the plaintiffs "sold short" some 5% of the total shares of the E. L. Bruce Company. In accordance with the discretion given in the American Stock Exchange's Rule 783, the Committee on Floor Transactions suspended trading in the issue and thereby allegedly injured those who had taken the short position. In denying the plaintiff's motion for a preliminary injunction, the Court held:

> The Exchange defendant has established rules and regulations. Its officers and committees apply those rules and regulations. This court cannot under the circumstances here revealed substitute its own view (even if so inclined) for that of the Exchange's own officers. The evidence does not reveal a "corner"

> of the Bruce stock in this situation. The Exchange's officers have not been able to make such a determination. Short of a patent fraud or obvious wrongful application of its constitution or regulations, the courts should leave such asscciations (stock exchanges) to apply their own regulations. (13 Misc. 2d at 1078-79, 178 N.Y.S. 2d at 959)

This concept has recently been reaffirmed in ***J. R. Williston & Beane, Inc.*** v. *Haack,* CCH Fed. Sec. L. Rep. ¶ 94,921 (S.D.N.Y. 1974), where the court said (p. 97,168), "The courts should be reluctant to substitute their hindsight judgment for that of those responsible for maintaining the integrity of the industry. . . ."

Because of the role played by the Exchange as a regulator, the Exchange must have the right to exercise good faith discretion in determining appropriate remedial action. When a possible infraction comes to the attention of the Exchange, it must weigh many interests. The imposition of drastic penalties might undermine investor confidence in the member. Certain disciplinary actions might jeopardize the accounts of the firm's customers when the infraction creates little risk to the member's ability to continue in business. There is a duty to protect customers, but also a duty to protect public investors who are not yet customers of the firm, but who may become customers if the sanction is slight. In addition, the interests of other firms who will continue to deal and to trade with the offending firm must be considered, as well as the general economy. There is also a risk of harm to the firm being disciplined if the sanction imposed is, in fact, too severe.

In the circumstances of this case, a private cause of action cannot lie in plaintiffs' favor for breach of statutory duty, *e.g., Baird* v. *Franklin,* 141 F.2d 238 (2d Cir.), *cert. denied,* 323 U.S. 737 (1944), or breach of a contract to a third party beneficiary, *e.g., Weinberger* v. *New York Stock*

Exchange, 335 F.Supp. 139 (S.D.N.Y. 1971). Liability against the Exchange could be imposed under such theories only if, after the Exchange learned of Weis' financial difficulties in mid-April 1973, the Exchange failed to take remedial action and such failure to act resulted in injury to plaintiffs. *Baird* v. *Franklin,* 141 F.2d at 239; *Steinberg* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.,* [1973-74 Transfer Binder] CCH Fed Sec. L. Rep. ¶ 94,599 at 96,122 (S.D.N.Y. 1974); *Marbury Management, Inc.* v. *Kohn,* 373 F.Supp. 140, 143 (S.D.N.Y. 1974). Neither prerequisite for establishing such liability is present on the uncontested facts of this case.

The Exchange, as this Court (Friendly, J.) recently noted in *United States* v. *Solomon,* Docket No. 74-2316 (2d Cir. filed Jan. 14, 1975), "commenced a full investigation on the following day" after notification of Weis' financial difficulties, despite the Weis "officers' urging that NYSE refrain, at least temporarily" (p. 2). When financial irregularities were discovered, the Exchange advised the SEC, in accordance with its statutory duty, "of the probable violations of its rules and regulations and began transmitting, on an almost daily basis, reports containing the results of its investigatory activities and contemplated actions." (*Id.*) Of course, the Exchange also communicated with SIPC. (Bishop 42) Plaintiffs' attack one of the remedial measures proposed by Weis, and approved by the Exchange, to improve Weis' net capital position. Pending negotiation and consummation of a proposed merger between Weis and Ladenburg, Weis suggested that "it transfer some of its larger margin accounts to Ladenburg in order to effect an automatic and immediate improvement of its debit capital ratio." (A 128a) The Exchange approved this suggestion, which was consistent with the objective of improving Weis' financial condition and achieving customer safety.

Plaintiffs fail to say why the transfer of margin accounts was an unreasonable or improper measure for the Exchange to approve. The transfer of margin accounts, which were financed by bank borrowings, would reduce Weis' liabilities and improve Weis' capital position. It would have been unfair to the stockholders, investors and creditors of Weis to have made no attempt to keep Weis in business, particularly before the full facts were known. It would have also been contrary to the Exchange's responsibility to maintain public confidence in the securities industry and member organizations of the Exchange. Moreover, the transfers of margin accounts could not prejudice the remaining Weis customers.

Mr. Julien conceded in his oral argument that the accounts to be transferred were "chosen at random." (Tr. 6) The reason why Weis chose to transfer its larger accounts need not "raise a suspicion in the court's mind" (App. Br. 62), because in the article that plaintiffs concede is authentic, it is explained that "a relatively few transfers would have a relatively large impact." (A 37a) Before the transfers were effected, Ladenburg had to pay to Weis the cash amount of any margin indebtedness. Thus, the plaintiffs' contention (Br. 9) that "if these accounts had not been transferred out, there would have been additional funds and securities available for the plaintiff and other Weis customers once the SIPC Trustee came in" is simply erroneous. The customers whose accounts were transferred out would have been entitled to share—had such transfers not been made—based upon the same mathematical formula that was applied to plaintiffs' accounts. The fact that the transferred accounts exceeded $50,000, which is the maximum protection provided under SIPC, would not alter the calculation of their pro rata share. As to those Weis customers within the $50,000 limit, however, such as plaintiffs and 99.5% of all other Weis customers, there was the absolute statutory assurance that they could not be damaged by such transfers.

Plaintiffs (Br. 36,60) would leave the exchange only two alternatives, an "immediate suspension" or disclosure "to everyone that Weis wished to have its margin customers transfer their accounts somewhere else or to tell no one." An immediate suspension may be appropriate in some circumstances for a clear and conceded violation of the Exchange's net capital rule, *e.g.*, *J.R. Williston & Beane, Inc.* v. *Haack*, CCH Fed. Sec. L. Rep. ¶ 94,921 (S.D.N.Y. 1974), but it is not required by the Exchange's Constitution. Article XIII, section 2 of the Exchange Constitution provides:

> Whenever it shall appear to the Chairman of the Board that a member has failed to meet his engagements, or is insolvent, or the Chairman of the Board has been advised by the Board of Directors of the Exchange or by the Board of Directors of Stock Clearing Corporation that such member is in such financial or operating condition that he cannot be permitted to continue in business with safety to his creditors or the Exchange, prompt notice thereof shall be given to the Exchange. Such member shall thereby become suspended from membership until he has been reinstated as provided in Section 5 of this Article. 2 NYSE Guide ¶ 1602 (1973).

Whether the remedy of suspension is necessary for the protection of creditors and customers is a determination that must be made by the Exchange. To have done so in the circumstances of this case, before the Exchange determined the extent of Weis' financial difficulties, and without trying corrective measures to improve Weis' financial condition, would have been an unconscionable response. A similar issue was recently considered in *Hughes* v. *Dempsey-Tegeler & Co.* [1973 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 94,133 (C.D. Calif), *appeal docketed*, No. 73-3591 (9th Cir. 1973), which also involved the role of

the Exchange in regulating a member organization which was facing serious capital problems. Mr. Hughes had subordinated his account with Dempsey-Tegeler in order to provide the firm with additional net capital. In finding that the Exchange had not violated its duties under section 6, the Court stated:

> And, although it was momentous, it was not an abuse of discretion, nor a violation of a statutory charge, for the Exchange to affirmatively solicit a subordination with the character, qualifications, and understanding, of that which was eventually consummated with Hughes. A contrary finding under the section 6 theory of recovery would appear to place national securities exchanges in an impossible position of making an ultimate choice between two alternative courses of action—either to submit themselves to a form of strict liability for the potential risks inherent in the type of protective scheme devised to preserve Dempsey, or to forego equally important obligations—legal *and* ethical—to other members of their national organizations and their clients. Such a choice does not seem to make sense under the Securities Exchange Act for it would at once remove fundamental flexibilities and discretions necessary for the effective functioning of natonal securities exchanges. (¶ 94,133 at 94,546-47)

Judgment was entered for the Exchange in *Hughes* after trial, but there, allegations of fraud and misrepresentation were also asserted against the Exchange. Plaintiffs in the instant action have conceded that the Exchange approved the transfers of margin accounts "to reduce the indebtedness of Weis & Company and apparently try to bring them up to an appropriate level," (Tr. 6), although in their brief to this Court, plaintiffs try to reverse themselves and to insinuate that such transfers might have been approved for "an illigitimate [sic] rea-

son." (Br. 51) Thus, unlike *Hughes,* on the uncontested facts of this action, neither the reasonableness of the method nor the Exchange's motive is in dispute. *Compare Kinzler* v. *New York Stock Exchange,* 62 F.R.D. 196, 202 (S.D.N.Y. 1974) (Gurfein, J.).

The other alternative plaintiffs would permit the Exchange is full disclosure of Weis' financial difficulties. Such disclosure would be inimical to the Exchange's effort to aid Weis. As the District Court so plainly saw, this would "create a run on the bank." (Tr. 18) Nothing in section 6 would suggest that the Exchange is forced to elect such a foolhardy measure in attempting to save a member or, alternatively, to take no action at all. An attempt to force disclosure of the Exchange's list of member organizations in financial difficulties and under Exchange surveillance was rejected in *Independent Investor Protective League* v. *New York Stock Exchange,* 367 F.Supp. 1376 (S.D.N.Y. 1973). Disclosure that Weis was experiencing financial difficulties could not have aided plaintiffs. The same shortages that required SIPC to advance funds would have resulted in many customers being unable to obtain all of the securities for transfer. No one would have benefited by such a pell-mell abandonment of Weis.

As the District Court noted, plaintiffs' attack on the reasonableness of the remedial measures approved by the Exchange amounts, in effect, to a claim, "that the rules of the Exchange were inadequate or unsuited to meet the problems Weis encountered, and that somehow, the Exchange should have acted differently." (A 137a) The District Court properly held that plaintiffs' relief for such a grievance is to apply to the SEC for a change in the Exchange rules pursuant to section 19(b) of the Exchange Act (15 U.S.C. § 78s(b)). In *Independent Investor Protective League* v. *New York Stock Exchange,* 367 F.Supp. at 1377, Judge Lasker said:

> If plaintiff wishes to influence or change Exchange policy, his remedy is to petition the SEC to exercise its powers under § 19(b) of the Act to recommend changes in Exchange rules, or to alter or amend the rules. The Administrative Procedure Act, § 4(d), 5 U.S.C. § 553(c) provides that "[e]ach agency shall give an interested person the right to petition for the issuance, amendment, or repeal of a rule." If plaintiff, is "aggrieved" by SEC action relating to Exchange rules, the APA § 10, 15 U.S.C. § 702 gives him the opportuntiy for judicial review.

See also Marbury Management, Inc. v. *Kohn*, 373 F.Supp. 140, 144 (S.D.N.Y. 1974); *Cutner* v. *Fried*, 373 F.Supp. 4, 9 (S.D.N.Y. 1974); *Kroese* v. *New York Stock Exchange*, 227 F.Supp. 519 (S.D.N.Y. 1964).

The remedial measure approved by the Exchange was clearly within the Exchange's broad discretion under section 6. As the District Court found, had the Exchange's efforts been successful, "no customers of Weis would have been damaged or inconvenienced in any way." (A 134a)

B. Transfers of margin accounts could not have damaged plaintiffs who were fully insured under the limits of the Protection Act.

In *Hughes* v. *Dempsey-Tegeler & Co., supra,* the court recognized that the Protection Act would "provide a mechanism by which such future crises would be avoided." (¶ 94,133 at 94,546 n. 29) The Protection Act "virtually eliminate[s] stockbroker bankruptcies as far as customers are concerned and replace[s] them with the faster and simpler operation of the liquidation proceeding." Note, *The Investor Protection Act of 1970: A New Federal Role in Investor Protection,* 24 Vand. L. Rev. 586, 612-13 (1971). For customers such as plaintiffs, and virtually all of Weis' other customers, with accounts within the insurance limits of the Protection Act, it would be un-

important whether the Exchange immediately shut Weis down or whether the Exchange adopted the remedial measures used in this case.

Had the Exchange suspended Weis in April, instead of May, plaintiffs appear to contend that "there would have been additional funds and securities available for the plaintiffs." (App. Br. 9) Inasmuch as plaintiffs obtained full recovery of the value of their accounts, such additional funds and securities would not be distributed to plaintiffs in any event. If plaintiffs are suggesting that the mix of securities and cash equivalent actually received by plaintiffs would have been different, that is obviously not a recoverable damage. Specific performance could not be directed against the Exchange, which did not hold the securities, so that plaintiffs' relief would necessarily be in money damages, which is exactly what plaintiffs received from SIPC.

The delay in processing plaintiffs' claim would be identical whether the SIPC proceeding occurred in April or May. Therefore, purported damages based upon profits that plaintiffs could have made on securities that they might have sold would be unaffected by the date that Weis was suspended. Also, the transfers of margin accounts reduced Weis' indebtedness, so possible damage to the remaining Weis customers was lessened. As the District Court stated:

> If some were caused to leave the sinking ship in time, this breach of duty, if it was one, neither caused nor exacerbated the injuries here complained of. Indeed, to the extent it helped Weis' finances, it may have expedited the SIPC reorganization, and mitigated the damage to Weis' other customers. (A 139a)

Plaintiffs are entitled to no recovery for an alleged breach of the Exchange's statutory duties where, as here, there

is no showing that the Exchange's actions were the proximate cause of damage to plaintiffs. *Baird* v. *Franklin,* 141 F.2d at 239.

C. The Exchange had no duty under Rule 10b-5 to disclose the transfers of margin accounts from Weis to Ladenburg.

The disclosure requirements of Rule 10b-5 cannot be construed to limit the Exchange's discretion under section 6. Having determined that the Exchange acted properly in approving transfers of margin accounts, it would be absurd to conclude that the Exchange is nevertheless liable to plaintiffs for failing to announce over the ticker tape the making of such transfers, where such an announcement would defeat the objective of saving Weis. *See Independent Investors Protective League* v. *New York Stock Exchange, supra.*

It is apparent that plaintiffs are attempting to assert a Rule 10b-5 claim in "defiance of reality," as the District Court suggested. (A 138a) This Court's decisions in *Shapiro* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.,* 495 F.2d 228 (2d Cir. 1974), and *SEC* v. *Texas Gulf Sulphur Co.,* 401 F.2d 833 (2d Cir. 1968), *cert. denied,* 394 U.S. 976 (1969), do not support such a claim.

A transfer of margin accounts is not a "purchase" or "sale" of securities within the meaning of Rule 10b-5 and the account itself is not a "security." Plaintiffs characterize the pro rata distribution by SIPC as forced sales of the unavailable securities, but as Mr. Giddens stated in his affidavit, "None of the securities shortages resulted from sales by the Trustee." (A 39a, ¶ 5) Thus, plaintiffs were neither purchasers nor sellers of securities, and only complain of a lost opportunity to transfer their Weis accounts which is not actionable under Rule 10b-5. As the Court of Appeals for the Ninth Circuit said when con-

fronted with an analogous flight of a plaintiffs' fancy: "There is not a scrap of authority supporting this extraordinary theory of Rule 10b-5 liability, and we will not supply any in this case." *Wessel* v. *Buhler*, 437 F.2d 279, 283 (9th Cir. 1971). Plaintiffs' tippee theory of liability against the Exchange should be similarly disposed of.

III

Plaintiffs, who have recovered the full value of their accounts with Weis, have no provable damages in fact or law.

There is no genuine issue of material fact that plaintiffs have no provable damages. It is undisputed that the plaintiffs each recovered the securities, or their cash equivalent, in respect of their brokerage accounts with Weis. Despite such recovery, plaintiffs have alleged, in paragraph 49 of the second amended complaint that

> by reason of the fact that WEIS was put into receivership, the plaintiffs had certain securities sold out for them by the receiver at prices which the plaintiffs would not have sold had they withdrawn their accounts from WEIS before WEIS was put into receivership and that the plaintiffs were unable to obtain their securities and trade in them and were otherwise damaged. (A 14a)

Defendants argued, *inter alia*, on the summary judgment motion that plaintiffs' claimed damages were speculative and not recoverable under this Court's decision in *Levine* v. *Seilon, Inc.*, 439 F.2d 328 (2d Cir. 1971). Moreover, it would be inconsistent with the purposes of the Protection Act to permit recovery against the Exchange of prejudgment interest for the administrative delays by SIPC in processing customer claims. Although the District Court did not reach this issue, in view of its determination that

plaintiffs failed to plead a valid cause of action, this Court can affirm on the ground that plaintiffs have no provable damages. *Perma Research & Development Co.* v. *Singer & Co.*, 410 F.2d 572, 575-76 (2d Cir. 1969); *Boston & Maine Corp.* v. *Chicago, Burlington & Quincy R. Co.*, 381 F.2d 365 (2d Cir. 1967), *cert. denied*, 390 U.S. 1027 (1968). *See also Helena Rubenstein, Inc.* v. *Bau*, 433 F.2d 1021, 1023 (9th Cir. 1970).

Plaintiffs claim (Br. 12-13) four elements of damage: (1) unspecified amounts for the period that plaintiffs were deprived of the use of their assets; (2) odd-lot commissions that plaintiffs might have to pay if plaintiffs sell securities allocated to their Weis accounts by SIPC; (3) brokerage commissions plaintiffs might incur to reacquire those securities unavailable from Weis in liquidation; and (4) tax consequences that one plaintiff would have preferred to realize in a year other than 1973. Each item is based upon conjecture and relates to profits, or expenses, that plaintiffs might have realized if they had done certain things, which they did not do and which under *Levine* they had no right to do.

As one plaintiff explained the first item of alleged damage, plaintiffs seek to recover unspecified sums based upon what they "could have done or what trading or investment [they] could have made with the money that [they] weren't able to get." (Schiff 233) Such speculative losses are not recoverable. See *James Wood Gen'l Trading Establishment* v. *Coe*, 297 F.2d 651 (2d Cir. 1961), where the plaintiff claimed damages based upon the failure of his broker to exercise an authorization to sell if the stock rose to 58. The court rejected the claim, stating:

> What proof can there be that . . . he would have sold . . . at 58⅛ or any other price? How can such a conclusion be arrived at other than by the merest guesswork and speculation. (297 F.2d at 658)

That Shurpin is "angry" (Shurpin 169-70) and testifies, "I *feel* that I have been wronged, and I would like to have it corrected. I *feel* that there is [sic] a lot of losses incurred which should not have been," (Shurpin 147) (emphasis added), cannot convert his claim into provable damages. The admission of Rich that his estimate of damage is based solely on "surmise" and no facts falls in the same category of speculative losses. (Rich 68)

In *Zirin Lab. Int'l, Inc.* v. *Mead-Johnson & Co.*, 208 F.Supp. 633 (E.D. Mich. 1962), the defendants' motion for summary judgment was granted on facts similar to these. Counsel for defendants in that case asked the plaintiff's president during his deposition to state the basis for plaintiff's claim for damages. He testified, "We feel we have suffered these damages." (208 F.Supp. at 636) Counsel then asked whether it was a fact that the estimate was based upon nothing more than his feeling and the president replied, "That is correct." (*Id.*) In dismissing the complaint, the court in *Zirin* stated:

> It would appear that "feeling" falls somewhere below "conjecture" and "guess" when measured by a rational standard. . . . If damages may not be estimated by guess or conjecture, a fortiori they may not be arrived at by a mere "feeling." (208 F.Supp. at 636)

Plaintiffs contend that they are entitled to recover odd-lot commissions that they might have to pay if they should ever decide to sell any of the securities received from SIPC. Of course, plaintiffs have not sold, as far as the instant record shows, and may never sell such securities. Such commissions may or may not be charged when and if they do sell. Prior to any sales, the plaintiffs may buy, or otherwise receive, aditional securities and thus hold round lots at the time they sell. If plaintiffs are charged odd-lot commissions at a future date, the rate cannot be predicted now.

Similarly, after they received their cash none of the plaintiffs attempted to reacquire in the market the securities unavailable from Weis. That plaintiffs express a longing to do so at a future date does not entitle them to recover brokerage commissions that might be paid. Furthermore, if plaintiffs had promptly mitigated their "damages" by covering the missing securities (for which plaintiffs received cash) when the price declined below the May 24, 1973 value they would have more than offset such commissions. Plaintiffs were obviously relieved to have been taken out of the market when they were.

Shurpin has clearly realized a tax benefit from his tax losses, resulting from the deductibility of those losses. He appears to be arguing, however, that if he ever realizes any "possible capital gains" (A 84a), he might have a greater tax benefit, by offsetting such capital gains against his losses, than the tax benefit he realizes by offsetting his losses against ordinary income. This amounts to a damage claim of conjecture based upon conjecture.

The District Court rejected plaintiffs' claim as too "speculative, remote or conjectural" (A 128a). It was less certain, however, whether plaintiffs would be entitled to interest for the alleged "wrongful failure to pay money when due." (A 129a) Defendants submit that plaintiffs' claim to interest as an item of damage is not different from the other speculative profits for which recovery is sought. First, the award of interest must be based upon the assumption that plaintiffs would have sold the securities in their accounts and would have invested in notes or savings banks giving them a return of interest. There is nothing in the record to support such an assumption.

Second, plaintiffs' interest claim, just as their other "profit" claims, are based on the assumption that their accounts, like those of the so-called privileged customers, would have been transferred out of Weis. In other words,

the plaintiffs' "lost profits" are attributable to transactions that they could have made if they had learned of Weis' financial difficulties and transferred their accounts. The Exchange Act clearly does not authorize recovery of damages posited upon such a theory. *Levine* v. *Seilon, Inc.*, 439 F.2d 328 (2d Cir. 1971). The plaintiff in *Levine* was a preferred shareholder of Seilon. He alleged that Seilon falsely represented it would proceed with an exchange offer of common for preferred stock thereby causing an increase in the market price of the preferred stock. For damages, the plaintiff claimed that he was "entitled to what he could have realized if he had sold his preferred stock at the inflated prices prevailing during the summer of 1968 . . . ." (439 F.2d at 333) The complaint, however, did not allege that Levine had any intention of selling his preferred shares during the summer or fall of 1968. Judge Friendly, writing for the court, held that the plaintiff had not suffered a compensable loss:

> Although he might have done so if he learned of Seilon's allegedly deceitful intent, he could hardly be heard to claim compensation for the premium he might have extracted from some innocent victim if he had known of the fraud and the buyer did not.[8]
>
> ---
>
> [8] In such a case, Levine would have stood in the posture of a "tippee" whose conduct . . . would be as reprehensible as his insider source. (439 F.2d at 333)

The plaintiff in *Levine* had also received the call price of his preferred shares, exactly what he was entitled to receive. The "suit was properly dismissed," therefore, "because on his own showing, he suffered no compensable loss." (439 F.2d at 335)

Similarly, here, if the plaintiffs had transferred their accounts out of Weis prior to May 24 on the basis of alleged inside information regarding Weis' financial difficulties—and thereby collected interest on their accounts—

plaintiffs themselves would have stood in the posture of "tippees." They would occupy the same status as those from whom they now demand recovery. Like Levine, plaintiffs do not allege that they had any intention of transferring their Weis accounts in April or May, 1973. Moreover, like Levine, the plaintiffs in this lawsuit admittedly recovered from SIPC exactly what they were entitled to. While the District Court recognized the significance of *Levine* on the issues of proximate cause, we submit that Judge Friendly's analysis of Levine's claim is equally applicable to the plaintiffs' attempt to recover interest here.

Taken together, the plaintiffs' claims of damages are but an illusion of damage—an attempt to equate "interest," on no damage, with damage as a matter of law, where plaintiffs received full recovery from SIPC. In such circumstances, there is no authority for awarding interest *in gross.*

The plaintiffs elected to file their claims in the SIPC proceeding. They accepted the SIPC checks in full satisfaction of those claims and are now barred from obtaining further recovery against the defendants. The right to recover interest is merely incidental to recovery on the underlying claim, which was extinguished upon acceptance of the SIPC checks. *Stewart* v. *Barnes,* 153 U.S. 456, 464 (1894) ("plaintiff has parted with his right of action by accepting the money which was withheld from him, and at the same time given up his right to sue for the incidental damages.") *cf. Cook* v. *United States,* 274 F.2d 689, 692 (2d Cir. 1968). In *Herzfeld* v. *Laventhol, Krekstein, Horwath & Horwath,* 378 F.Supp. 112, 129 (S.D.N.Y. 1974), Judge MacMahon denied plaintiffs' claim to interest as damage, stating as follows:

> The Herzfelds' interest claims amount, essentially, to the interest they expected to receive on the notes from FGL. Thus, the interest was part of the profit they expected to make from their investment.

It would defeat the congressional purpose of the Protection Act if the delays attributable to SIPC in processing customer claims could become the basis of a damage claim against defendants. In this case judicial action was commenced by SIPC against Weis on May 24, but a SIPC trustee in liquidation was not appointed until May 30. (A 38a, ¶ 2) During those six days, as contemplated by Congress, further efforts were made by the responsible regulatory agencies to keep Weis in business. Unfortunately, those efforts were unsuccessful, but to ensure that no unfairness would result to customers based upon market fluctuations, the valuation date was established by law as May 24. Protection Act § 5(b)(4), 15 U.S.C. § 78eee(b)(4). If it is determined that the plaintiffs are entitled to recover interest for such necessary delays, there will never be any attempts to take corrective steps short of liquidation. Moreover, it would be an extraordinary application of the law of damages to hold defendants liable for interest based upon mechanical delays in processing 35,000 customer claims by SIPC.

Furthermore, most of the SIPC funds used to compensate plaintiffs and other Weis customers come from assessments against registered broker-dealers (Protection Act § 4(c), 15 U.S.C. § 78ddd(c)), most of which are members of the Exchange. To further surcharge the Exchange, a not-for-profit corporation made up of those member organizations, would be contrary to the principles of equity and fairness. See *Board of Comm'rs* v. *United States,* 308 U.S. 343, 352 (1939) ("The cases teach that interest is not recovered according to a rigid theory of compensation for money withheld, but is given in response to considerations of fairness. It is denied when its exaction would be inequitable.").

Plaintiffs professed concern (Br. 54) about the "colossal fraud . . . by one of the Exchange's larger members with over 35,000 customers" might be understandable if plaintiffs had not received full recovery of the value of their Weis' accounts, along with apparently all but 70 other

customers. (A 37a) In the context of the absence of damages, plaintiffs' attack on the good faith of the Exchange and Ladenburg is but a hollow claim surrounded by an aura of greed.

CONCLUSION

On the statement of plaintiffs' attorney that there was no substantial disagreement as to the facts, the District Court was entitled to enter summary judgment for defendants on a ground not urged. The District Court correctly determined that the Exchange properly discharged its statutory duties in its efforts to aid Weis and that such actions as the Exchange approved could not be the proximate cause of damage to plaintiffs. Moreover, on this record plaintiffs have no provable damages in fact or law. The purpose of summary judgment is to pierce conclusory allegations and dispose of unsupportable claims prior to trial. That purpose has been achieved in this case. The judgment of the District Court should be affirmed.

Respectfully submitted,

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February 3, 1975

UNITED STATE COURT OF APPEALS

FOR THE SECOND CIRCUIT

- x

NORMAN RICH, et al.,	:	
Plaintiffs,	:	AFFIDAVIT OF SERVICE
-against-	:	
NEW YORK STOCK EXCHANGE, et al.,	:	
Defendants.	:	

- x

STATE OF NEW YORK)
: ss.:
COUNTY OF NEW YORK)

NED B. BERTULFO, being duly sworn, deposes and says:

I am over the age of 18 years and am not a party to this action.

On February 3, 1975, I served the within briefs on the attorneys listed below by depositing two true copies thereof, securely enclosed in post-paid wrappers addressed to each of such attorneys at their respective addresses in a mailbox maintained by the government of the United States in the City of New York.

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Sworn to before me this

3rd day of February, 1975.

Louis A. Wolf

LOUIS A. WOLF
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Qualified in Nassau County
Certificate Filed in New York County
Commission Expires March 30, 1976